

BEFORE THE STATE BOARD OF EQUALIZATION
OF THE STATE OF CALIFORNIA

In the Matter of the Appeals of)
O.S.C. CORPORATION, ET AL.) Nos. 79A-22 and 83A-63-KS

Appearances:

For Appellants: Willard D. Horwich
Attorney at Law

For Respondent: Jon Jensen
Counsel

O P I N I O N

These appeals are made pursuant to section 25666^{1/} of the Revenue and Taxation Code from the action of the Franchise Tax Board on the protest of O.S.C. Corporation, et al., against proposed assessments of additional franchise tax in the amounts and for the income years as follows:

1/ Unless otherwise specified, all section references are to sections of the Revenue and Taxation Code as in effect for the income years in issue.

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against the parent corporation's income, and resulted in the proposed assessments for those years.

In an unrelated transaction, appellant settled a lawsuit for \$130,000 during its 1976 income year that it had brought against Toshiba America in 1971. The suit charged Toshiba with various violations of the state and federal anti-trust laws as well as breach of contract. Based upon documents provided by appellant, respondent concluded that the majority of the settlement was related to lost profits, which are taxable as income, and should have been reported as income during its 1976 income year.

Appellant protested all of respondent's determinations, respondent denied the protests, and this appeal followed.

We begin with the issue of combined reporting. Section 25101 requires a taxpayer deriving income from sources both within and without this state to measure its franchise liability by its net income derived from or attributable to sources within this state. If the taxpayer is engaged in a single unitary business with affiliated corporations, the income attributable to California sources must be determined by applying an apportionment formula to the total income derived from the combined operations of the affiliated companies. (Appeal of the Amwalt Group, Inc., formerly Allan M. Walter and Associates, Inc., Cal. St. Bd. of Equal., July 28, 1983.)

The California Supreme Court has set forth two alternative tests for determining whether a business is unitary. In Butler Bros. v. McColgan, 17 Cal.2d 664 [111 P.2d 334] (1941), affd., 315 U.S. 501 [86 L.Ed. 991] (1942), the court held that the existence of a unitary business was definitely established by the presence of the unities of ownership, operation, and use. Later, in Edison California Stores, Inc. v. McColgan, 30 Cal.2d 472 [183 P.2d 16] (1947), the court held that a business is unitary if the operation of the business done within this state depends upon or contributes to the operation of the business outside the state.

Respondent accepts the unitary nature of appellant's corporations for the income year 1975 when one of its subsidiaries conducted business outside of this state. Respondent apparently based its assessment for that income year on other grounds. Although appellant filed an appeal against that assessment, it advances no

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right, at least for income years beginning prior to 1980,^{2/} to file a combined report and be treated as a unitary business, even though they would have been considered as such had the business activities been interstate.

Appellant takes the position that California Administrative Code, title 18, regulation 24303, which provided the rules for combined reporting, was the basis for the Handlery decision. Accordingly, appellant contends that the subsequent repeal of regulation 24303 changes the Handlery rule.

This attempt to discredit the Handlery decision is misguided. As stated by respondent, the repeal of regulation 24303 would not change the result of Handlery because the decision was based upon other authority. A cursory reading of the opinion reveals that the only reason the regulation was discussed was because the appellant in that case argued that the regulation, combined with section 25102, made combined reporting discretionary. That argument was rejected by the court. Consequently, we find that appellant has not shown why it should be entitled to file combined reports for the years at issue.

Appellant demands that if we find that respondent was correct in requiring separate returns for each corporation, this board must make an allocation of income and expenses between the corporations. It is not the province of this board to do as appellant requests, however, because such an allocation is solely within the discretion of the Franchise Tax Board. (Rev. & Tax. Code, § 24725.)

2/ Section 25101.15, enacted by chapter 390 of the 1980 Statutes, permits intrastate "unitary" businesses to file combined reports for income years beginning on or after January 1, 1980. Consequently, it is of no assistance to appellant here. Section 25101.15 provides:

If the income of two or more taxpayers is derived solely from sources within this state and their business activities are such that if conducted within and without this state a combined report would be required to determine their business income derived from sources within this state, then such taxpayers shall be allowed to determine their business income in accordance with Section 25101.

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Appellant argues that the settlement cannot be taxed as income received during its 1976 income year because an exception to this rule is provided by section 24678, subdivision (a), which states that:

If an amount representing damages is received or accrued during an income year as a result of an award in, or settlement of, a civil action [brought under the anti-trust laws commonly known as the Clayton Act] . . . then the tax attributable to the inclusion of such amount in gross income for the income year shall not be greater than the aggregate of the increases in taxes which would have resulted if such amount had been included in gross income in equal installments for each month during the period in which such injuries were sustained by the bank or corporation.

Appellant contends that since the case was grounded in an anti-trust violation, the settlement appellant received should be treated in accordance with section 24678.

We note that section 24678 is applied exclusively to anti-trust actions. (Rev. & Tax. Code, § 24678, subd. (a).) Upon review of the complaint filed in the above-mentioned case, it is apparent that there are two causes of action alleged by appellant: an anti-trust action and a breach of contract action. The settlement agreement makes no mention of how much or to which cause of action the settlement should be applied. Appellant has not provided any information as to the amount of the settlement, if any, which may take advantage of section 24678. Without such information, we are unable to apply section 24678 to any of appellant's settlement. Therefore, respondent's action including the entire settlement amount as income during the income year 1976 must be sustained.

Finally, appellant contends that it should be relieved of interest on the tax because of the time involved in awaiting the result in the federal tax litigation mentioned above and delays in receiving respondent's replies to appellant's briefs. We disagree.

As stated in Appeal of The Inn at La Jolla, Inc., decided by this board on December 18, 1964:

Section 25901 of the Revenue and Taxation Code provides, in mandatory language and without

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O R D E R

Pursuant to the views expressed in the opinion of the board on file in this proceeding, and good cause appearing therefor,

IT IS HEREBY ORDERED, ADJUDGED AND DECREED, pursuant to section 25667 of the Revenue and Taxation Code, that the action of the Franchise Tax Board on the protest of O.S.C. Corporation, et al., against proposed assessments of additional franchise tax in the amounts and for the income years as follows:

<u>Appellants</u>	<u>Income Years Ended</u>	<u>Assessments</u>
O.S.C. Corporation	3/31/75	\$ 4,849.99
	3/31/76	33,288.16
	3/31/77	9,599.00
	3/31/78	35,909.00
Galaxy Stores, Inc.	3/31/77	200.00
	3/31/78	200.00
O.S.C. Corporation of California	3/31/77	200.00
	3/31/78	200.00
National Market Search, Inc.	3/31/77	200.00
	3/31/78	200.00

be and the same is hereby sustained.

Done at Sacramento, California, this 3rd day of December, 1985, by the State Board of Equalization, with Board Members Mr. Collis, Mr. Nevins, and Mr. Harvey present.

_____	, Chairman
Conway H. Collis	, Member
Richard Nevins	, Member
Walter Harvey*	, Member
_____	, Member

*For Kenneth Cory, per Government Code section 7.9